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THE CPA's VITAL ROLE IN ESTATE PLANNING

All too often, CPAs do not participate in clients' estate planning through failure to educate clients as to the value of their input. The absence of such participation leaves the process woefully incomplete, however, and there are compelling reasons why clients and their estate planning attorneys should seek the continuing help and supervision of CPAs in this process. Following are some of these reasons and suggestions as to the form such participation might take.

Continuing relationships

Individuals contact attorneys infrequently during their lifetimes, mostly for discrete, finite projects. Accountants, on the other hand, see their clients annually at a minimum, often at least quarter-annually, and develop ongoing personal relationships.

The attorney must seek information essential to the selection of the appropriate estate planning techniques for a particular client. This information would include the client's present and prospective net worth, asset mix, present and future cash flow needs, and family concerns (both financial and non-financial). Ordinarily, the CPA is the only party who maintains this information for the client. In addition, clients are comfortable and familiar with the quantitative tutoring they receive from their accountants, making the subject of sound estate and gift planning easily broached.

Accountants have regular access to clients' personal information and can determine whether they are complying with estate plans already in force. Clients tend not to consult attorneys after the initial preparation of estate planning documents, until a death occurs, and the attorneys cannot be so vigilant in making sure clients are not taking actions inconsistent with the estate plans. Nowhere does such a deficiency have more adverse results than in probate avoidance.

In many states, probate may be avoided upon death by means of a revocable living trust, but only if the trustors formally transfer title to their wealth, prior to death, from their individual names to themselves as the trustees. Because CPAs regularly see clients' property tax statements for newly acquired real property and Forms 1099 for securities and bank accounts, they are better able than attorneys to determine (from the title listed on such forms) whether clients who have current revocable living trusts have taken title to recently acquired property and/or accounts in the trust or, instead, in their individual names.

Practice development and continuity

It goes without saying that gift and estate planning considerations are relatively untapped areas for CPAs, since virtually every client can be helped by an introduction to such planning. In addition, it makes sense for the CPA to understand a client's basic estate plan, because after the client's death, the CPA's participation in the division and adminis-

(continued on page 7)

What's Inside . . .

Individual Accounting Practices: A Ten-Year Review (Part 2)

In the first part of this article, in the March Practicing CPA, *we met Leslie Peddy, an individual practitioner, and discussed the growth in firms' revenues over the past decade. We also measured the changes in owners' income when adjusted for price inflation during the period. This part will focus on sources of firm revenue and personnel costs.*

Sources of firm revenues

A trend we have long been watching is the amount of revenue independent practitioners realize from the major revenue sources—taxation, compilation and review, and auditing services. The shifts can be seen in exhibit 6. (Other revenue sources have remained almost constant, and thus, are not presented.)

In 1982, 72 percent of the practices' revenues were generated by these three sources. By the end of 1991, the figure had dropped to 69.7 percent. More important, however, is the shift in importance of each of these sources. At the beginning of the decade, 11.9 percent of revenue came from audit engagements. By 1991, that figure had declined to 6.9 percent, making audit fees a relatively minor contributor in most individual practice units. In fact, each year has seen a growth in the number of firms which do no audit work at all. Even compilations and reviews have become less important over the years. In 1982, 21.7 percent of firm revenues came from compilations and reviews, but this was down to 15.5 percent ten years later.

The real growth center has been in income tax services. If the trend continues, we should soon see half or more of firmwide revenues in individual practices generated by tax work. In a few individual practices, tax work, including tax advising, now makes up over 80 percent of revenues.

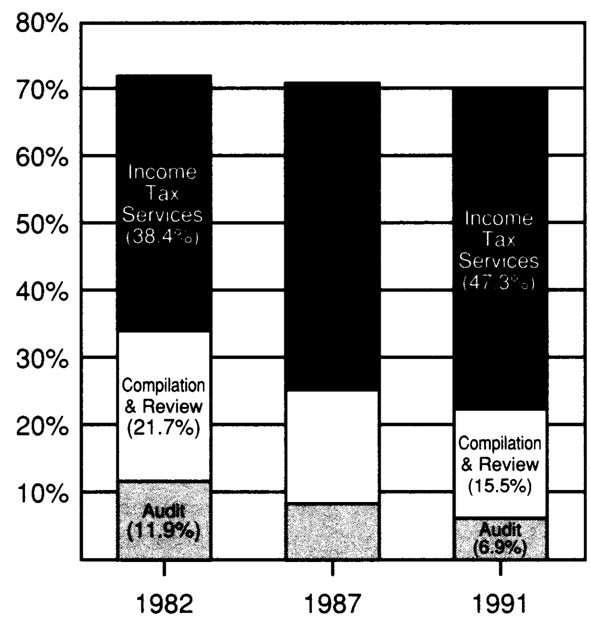
Personnel costs

Personnel costs are the most significant cost of operating a public accounting practice. In 1991, staff salaries (not including owners' incomes) and related costs amounted to 30 percent of revenues. Back in 1982, staff salaries were closer to 33 percent of revenues. In studying survey data, it appears that compensation costs have generally been squeezed most to realize cost savings for the firm.

Exhibit 7 shows average W-2 compensation for three levels of professional staff grouped as (a) managers and supervisors, (b) seniors, and (c) juniors. (We will refer to group (a) as "managers.") The compensation of juniors covers an eight-year span in exhibit 7 because a change in the survey made the results for 1982 and 1983 noncomparable with subsequent data.

The most noteworthy fact emerging from exhibit 7 is that compensation for all three groups did not keep abreast of inflation. In 1982, managers and seniors were paid an annual average of $29,396 and

Exhibit 6
Sources of Firm Revenues — Income Tax, Compilation & Review, Audit (1982, '87, '91)



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$22,790, respectively. By 1990, they were being paid as follows: managers, $38,117, and seniors, $28,941, representing increases during the decade of about 29.7 percent and 27 percent, respectively. During the eight years between 1984 and 1991, juniors' pay increased also, about 24 percent. Adjusted for price changes, managers', seniors', and juniors' actual annual pay were running behind the price level adjusted compensation by approximately $4,700, $4,200, and $1,900, respectively.

Exhibit 8 provides another vantage point from which to look at W-2 wages, this time as ratios of one group to another. The wages of seniors were compared with managers' in each of the ten years and are shown as line A. In 1982, the quotient was a little below 78 percent, fell to 74 percent in 1985, rose to slightly over 80 percent in 1987, and ended the decade at 76 percent, little changed from ten years before.

Wages of the junior professional staff were compared to seniors' wages and are shown as line B. This begins in 1984, as previously explained, and hovers near that level for most of the decade. At the highest point, in 1989, juniors were paid slightly over 79 percent of seniors' salaries.

A slightly different pattern emerges in line C, which shows the wages of managers compared to the income of owners. From 1982 to 1986, managers' earnings were about 60 percent of owners' incomes.

Exhibit 7
Average Annual W-2 Compensation Actual and Adjusted (1982 – 1991)

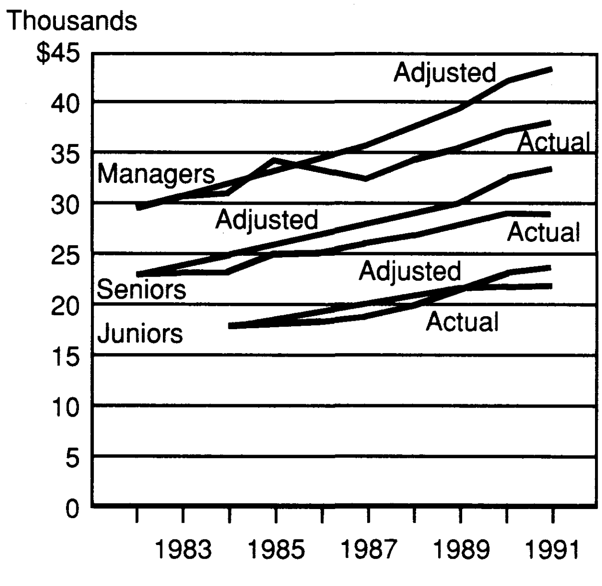
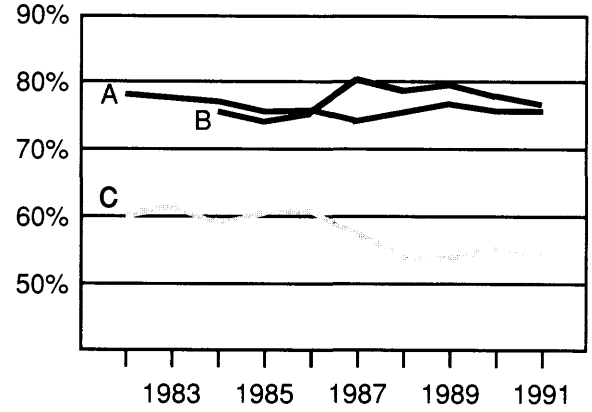


Exhibit 8
Ratios of W-2 Wages (1982 – 1991)



A — Wages of seniors compared to wages of managers
B — Wages of juniors compared to wages of seniors
C — Wages of managers compared to owners' income

The quotient fell to 57 percent in 1987 and still further to 54 percent in 1991.

What can we make of these statistics? Is this an indictment of "trickle down" economics? We have placed our finger on the one area where the individual practitioner realized the greatest cost savings from 1982 onwards—professional staff salaries. In 1982, professional staff W-2 compensation (excluding owners' incomes) amounted to 18.3 percent of firm revenues. It dropped to 17.7 percent a year later, and ended 1991 at 15.7 percent.

This may be a good time to look back to exhibit 1 for a related matter—the number of people employed by the firm. The 1991 firm is leaner in number of personnel compared to its 1982 counterpart. By 1991, the average firm was smaller by half a person and the 25 percent most profitable firms had trimmed personnel by .8 of a person. While this does not seem like much downsizing, remember that reducing the staff of an average individual practice from 3.5 in 1982 to 3.0 people by 1991 is almost a 15 percent reduction. This is the equivalent of an office of 200 people being reduced to 170.

Summary

Where does this leave Leslie Peddy, CPA, and other individual practitioners, and those who are considering becoming individual practitioners? These practice units are changing the focus of services, departing the "bread and butter" services of auditing and compilations and reviews, while spending correspondingly more time providing tax services to clients. In addition, the last ten years have seen the average firm working hard in an attempt to stay even with the modest inflation being experienced in the economy.

Firms have become leaner (or more efficient, if that expression is preferred) from the standpoint of trying to do more with fewer people. While owners are maintaining an increase in firmwide revenues and their own income levels at a pace somewhat behind the rate of inflation, this is being achieved by savings in the cost of maintaining other personnel on the payroll. The individual practice unit is getting by in 1991 with 15 percent fewer employees than a decade before.

The picture is far from bleak. Firms have slimmed down, but the fact that they are operating at or near the purchasing power margins of a decade before is not bad. And some of the firms in the top quartile have prospered far beyond what many would have considered possible. Other firms, undoubtedly, have not fared so well.

What accounts for the difference in success between firms? Entrepreneurial zeal on the part of the owner? Location? Marketing efforts? All these factors and many more serve to make a profitable accounting practice. What the past decade has shown is that a firm can't stand still. Many organization textbooks say a firm must grow if it is to continue to prosper, but the Management of an Accounting Practice Survey has caused us to restate the axiom: A firm must adapt if it is going to stay in the race.

Pleasant dreams, Leslie. ☑

—*by* **Carlton D. Stolle, CPA,** Ph.D. *Texas A & M University, College of Business Administration, College Station, Texas 77843-4353*

National Accounting and Auditing Advanced Technical Symposium

The AICPA will hold its sixth annual National Accounting and Auditing Advanced Technical Symposium (NAAATS) on June 24–25 at Stouffer Harborplace, Baltimore, Maryland, and on July 12–13 at the Sheraton Palace Hotel, San Francisco, California. With the strong involvement of former and current members of the private companies practice section technical issues committee (TIC), the symposium is firmly focused on providing training and advice on advanced accounting and auditing issues to the partners of local and regional firms.

NAAATS participants can interact with standard setters from the Financial Accounting Standards Board, the Auditing Standards Board, and the Securities and Exchange Commission; discuss recent accounting and auditing pronouncements at a TIC roundtable; and attend sessions on fraud auditing, business health check-up, employee benefits, emerging issues in the government sector, legal liability, FASB 107 and 109, environmental issues, business ethics, and the COSO report on internal controls. Two optional evening sessions will deal with the duties of a professional and using the AICPA practice manual system.

For information or to register (fee $545), call the AICPA meetings and travel department, (201) 938-3232. ☑

AICPA National Practice Management and Firm Administration Conference

The AICPA National Practice Management and Firm Administration Conference, which focuses on helping partners, individual practitioners, and firm administrators enhance firm efficiencies and profits, will be held on July 19–21 at the Capital Hilton in Washington, D.C.

The sessions will cover planning and implementing profit strategies, current issues in employment law, managing the multi-office firm, the basics of forensic accounting, how to improve your decision-making skills, the latest practice management software, designing a cost-effective training program, running your firm like a business, technology planning, successful approaches to partner compensation, expanding the role of the firm administrator, partner retirement alternatives, providing services to construction clients, creating a marketing culture, the business of paradigms, effective communication, providing services to healthcare professionals, and reinventing your firm.

In addition to the presentations, registrants can participate in training sessions on AICPA software and manuals, and open forums for partners and firm administrators.

The registration fee is $595 (recommended for up to 22 hours of CPE credit). For more information, contact the AICPA meetings department, (201) 938-3232.

Your Voice in Washington

AICPA Supports Bill to Repeal Current Estimated Tax Rules

When Congress, in 1991, changed the way certain individual taxpayers must calculate their quarterly estimated tax payments, the AICPA warned Congress not to do it because it would make the process unworkable. By now, many taxpayers probably wish Congress had heeded the AICPA's advice. They have discovered it's impossible to comply with any assurance that they will avoid an estimated-tax penalty.

The AICPA has supported efforts to ease the effects of the new law from the first day it was enacted. Unfortunately, during the last Congress, the measure endorsed by the AICPA was changed so significantly from its original form that the AICPA had to withdraw its support. In its unacceptable form, it was passed as part of a tax bill President Bush later vetoed.

The bill to repeal the estimated tax rules introduced this April by Senator Dale Bumpers (D-AR), S. 739, reflects the thrust of the changes recommended to Congress by the AICPA — that a measurable safe harbor be restored to the calculation of estimated taxes for unincorporated businesses and certain individual taxpayers.

Specifically, S. 739 would

- ☐ Permit taxpayers who now use the 100 percent previous-year tax safe harbor to keep using it.
- ☐ Restore an estimated-tax safe harbor based on a *previous*-year tax liability to taxpayers who lost their safe harbor when the 1991 law was implemented.
- ☐ Require some taxpayers with income above $150,000 to use 110 percent of their previous year's tax liability (rather than 100 percent) as a safe harbor.

Outlook

The AICPA believes S. 739 has a credible chance of being enacted into law. In addition to the fact that Congress already wrangled with this issue last year, the problems taxpayers encountered during the filing season may fuel grassroot resentment. Particularly if taxpayers express their frustrations to their House and Senate members, the opportunity for change will increase.

Senator Bumpers, who is chairman of the Senate Small Business Committee, and Senator Orrin Hatch (R-UT), who is both a co-sponsor of the bill and a member of the Senate Finance Committee, are encouraging their Senate colleagues to include S. 739 as a part of any tax bill passed by Congress this year.

The AICPA, and the other business and professional organizations that support S. 739, also will continue to push for the bill's enactment. ☑

Conference Calendar

MICRO93–Microcomputer Conference and Exhibition
June 13–16—The Sheraton Boston & Towers, Boston, MA
Recommended CPE credit: 20 hours

National Accounting and Auditing Advanced Technical Symposium
June 24–25—Stouffer Harborplace, Baltimore, MD
July 12–13—Sheraton Palace, San Francisco, CA
Recommended CPE credit: 16 hours

Employee Benefits
June 28–29—The Capital Hilton, Washington, DC
Recommended CPE credit: 16 hours

Not-for-Profit Conference
July 8–9—Grand Hyatt, Washington, DC
Recommended CPE credit: 16 hours

Healthcare Conference
July 19–20—Bally's Casino Resort, Las Vegas, NV
Recommended CPE credit: 16 hours

National Practice Management and Firm Administration Conference*
July 19–21—The Capital Hilton, Washington, DC
Recommended CPE credit: 22 hours

CPA's Role in Litigation
July 22–23—Hyatt La Jolla, La Jolla, CA
Recommended CPE credit: 16 hours

Estate Planning Conference
July 28–30—Sheraton Palace, San Francisco, CA
Recommended CPE credit: 24 hours

Small Firm Conference*
August 18–20—Sheraton Palace, San Francisco, CA
Recommended CPE credit: 23 hours

National Governmental Accounting and Auditing Update Conference
August 30–31—Grand Hyatt, Washington, DC
Recommended CPE credit: 16 hours

To register or for more information, call the AICPA CPE division, (800) 862-4272.

*Call the AICPA meetings and travel department, (201) 938-3232.

Death in the Firm

Two and a half years after the formation of our two-partner accountancy corporation, my partner died suddenly in March 1991, of a stroke. Immediately, there were several crises and problems that needed to be confronted and solved if the corporation was to survive as an entity.

Obviously, my professional workload had been doubled, and previous goals and plans, which were based on the collective strengths of two people, were neutralized. Now 100 percent in charge of the administrative and professional life of the firm, I would have to decide whether to sell, merge, or continue operations as a sole practitioner.

The existence of a buy/sell agreement and two life insurance policies seemed comforting. We had entered into a buy/sell agreement wherein insurance policies on each partner's life were purchased by the corporation, with the corporation as the beneficiary, and with an agreement specifying that the proceeds would be used to purchase part of the deceased partner's share in the corporation. The agreement also specified that additional funds would be paid to the extent of 75 percent of the prior year's billings divided by the number of shares outstanding, less the amount of the insurance proceeds.

In retrospect, the terms of our agreement were not favorable to the surviving partner. While I strongly recommend that all firms have buy/sell agreements with insurance coverage to fund a portion, if not all, of the buyout of the deceased partner's interest in the organization, I believe outside professional assistance should be used when negotiating terms, to ensure fairness to all concerned.

My primary concern was to stem client loss. In the year following my partner's death, client attrition amounted to approximately 20 percent of total billings in the first six months, and had reached one-third of prior billings by the end of 1992. There were several reasons for this.

Client loss

On joining the firm in 1988, I was placed in charge of all new clients and those clients to whom we provided management and computer consulting services. I was also responsible for staff supervision relating to accounting work and tax-return preparation.

My partner, who retained the old-line clients (the financial backbone of the firm), specialized in personal financial planning and performed some management and administrative duties. The client base was composed, primarily, of doctors and attorneys.

On my partner's death, I immediately notified clients through letters and phone calls that he and I had worked closely in the preparation of their tax returns and accounting services, and that the prior level of service would continue. Because it was the beginning of tax season, most clients did not wish to select a new accountant on such short notice and elected to stay temporarily with the firm.

My partner, however, had established strong personal and professional relationships with most of the old-line clients. I had been involved in aspects of the services they received but had never solidified relationships with them. Consequently, they did not view me as their accountant. There had been no plan to introduce me to these clients when I joined the firm. That failure ultimately caused a loss of clients that might have been avoided.

This experience demonstrates the need for partners to clearly identify their relationships with the clients for whom they are responsible. The financial repercussions of the loss of a partner should then be evaluated by all the partners in terms of these relationships. This is particularly important in a small professional office of five or fewer partners.

Goals and plans affected

The firm's professional services product mix and revenue sources were distributed equally among small-firm accounting services and individual and corporate tax returns. Computer and management consulting services provided substantial contributions to firm revenues during the off-season. The firm had experienced solid growth through the addition of these services and the purchase of a small accounting firm. We had also begun implementing an organized marketing plan directed by a company specializing in developing new business for CPA firms.

Our firm had specialized in providing services to the healthcare industry, primarily to doctors and nurses. We planned to expand services to this group and develop new products, such as general financial consultations for medical practices, the design and installation of internal control systems, and the training of medical practice staff in the implementation of proper billing procedures.

These plans were based on my partner's expertise in the healthcare industry, and his relationship with most of the doctors. Without the key relationships in place for me, all these marketing strategies had to be placed on hold.

The addition of so many more responsibilities initially placed such severe demands on my time that new business development was effectively stalemated. I determined that once the situation stabilized, I would need to reassess the direction the firm was headed in and cultivate a more diversified client base. I realized I was faced with developing a whole new view of the surviving company, its philosophy, its service levels, and the desirable types of client to seek. For continued survival of the firm, it was crucial to identify ways to replace clients who were likely to leave.

Since that first calamitous year as an unprepared sole practitioner, I have merged with three other CPAs. Our new firm is implementing procedures such as regular partner meetings and combined marketing plans. We have reduced the firm's exposure to the healthcare field and have broadened the scope of new business development activities to other areas.

To avoid the situation I found myself in, I suggest you establish a marketing plan that every partner is committed to and which can still be executed in the event of partner loss. ☑

—*by* **Warren Nogle, CPA,** *McLoughlin, Briese, Yip & Nogle, 100 Spear Street, Suite 1630, San Francisco, California 94105, tel. (415) 882-7373*

PCPS Advocacy Activities

Directory of AICPA member benefits and services available

The private companies practice section (PCPS) of the division for CPA firms has recently developed a directory of AICPA programs and services that helps CPAs in public practice get the most value from their AICPA membership. From technical and research assistance to help with common problems, the Institute has much to offer practitioners.

To obtain a complimentary copy of the directory, call the PCPS staff, (800) CPA-FIRM.

TIC sponsors joint AICPA/RMA task force

The PCPS technical issues committee (TIC) has sponsored a joint AICPA/Robert Morris Associates (RMA) task force to formalize a loan-submission package. Representatives of the two groups have met to explore the possibility of developing a common ground on the presentation of financial information for small business loan applications.

From the TIC's perspective, agreement with lenders on necessary financial information could help small businesses to obtain quicker loan approval. From RMA's perspective, lenders would be able to make decisions on a common basis of minimum financial information presented in a consistent manner.

The task force will present a proposed loan-submission package to both the AICPA and RMA for approval.

CPA's Role in Estate Planning
(continued from page 1)

tration of assets could provide a smooth transition to representation of a surviving spouse and, later, the next generation.

This phenomenon is prominent in the passage of ownership in a family business down to the children of the original owners. In fact, the level of a CPA's participation in the transition may dictate whether he or she is asked to continue in representing the enterprise.

Following are some ways CPAs can provide substantial services to clients in the areas of gift and estate planning.

Gift-giving program. Accountants can determine the estate and gift tax savings, and the drainage of assets otherwise available for clients' future needs, which can result from gifting options. In addition, CPAs are best qualified to evaluate basis and income-shifting considerations in selecting the assets for a gift program.

Trust administration. Many estate planning techniques utilize irrevocable trusts. These vehicles require a constant vigil, because clients tend to neglect the formalistic requirements of such separate legal, taxable entities. Segregation of assets and records, protecting trust assets from the client/trustor's access, and notifying beneficiaries of trust assets are just some of the requirements often neglected by an incompetent trustee. The CPA, who should prepare accountings and tax returns for the trust, has the long-term relationship with the client and the client's family, as well as a strong business and quantitative background, and is often the logical choice to serve as trustee of such a trust.

Revocable living trusts may not require the CPA as initial trustee. The accountant may, however, be an appropriate successor trustee, especially under circumstances where clients are living but incapable of handling the totality of their wealth. As stated above, CPAs can continue to monitor whether effective probate avoidance techniques are being administered correctly by clients.

Life insurance needs. CPAs are aware of the lifestyle and savings practices of their clients, and may be uniquely suited to understand their clients' life insurance needs, considering (1) the cash-flow drop which a death will bring as a result of lost income of a deceased spouse and (2) the liquidity needs to pay estate tax. Often, a business can only survive the death of a major shareholder/employee with careful planning. The CPA, who regularly observes and advises the principals of a family business, can evaluate the client's needs for buy–sell or redemption arrangements (another place where life insurance may be appropriate) and participate in the creation of business continuation contingency plans.

Post-death involvement. After a client's death, the involvement of the CPA can be extremely important to the effectiveness of the estate plan. The estate tax returns of a decedent require fair market value information for all of the decedent's assets, and often the accountant has the greatest access to this information. Further, many estate plans require allocation of assets among several trusts which have different distribution schemes and different future estate tax characteristics. The CPA's understanding of the client's asset mix, as well as the appreciation potential of particular assets, can be invaluable in this allocation/selection process.

In addition, in many states, the probate process, if unavoidable, may be an involved proceeding, often requiring court-approved accountings for estates, and sometimes trusts. The obvious choice for the preparation of such accountings is the family CPA.

How to increase your estate planning involvement

In most areas, the estate planning community comprises mainly attorneys, life insurance agents, and financial planners. An excellent way to meet these professionals and create a network for information sharing and referrals is to invite them for speaking engagements at local CPA society meetings. You might also inquire about the current status of clients' estate planning and the identity of the professionals working with them. You can then contact these individuals and offer your participation.

If you wish to increase your familiarity with various estate planning concepts and techniques, try attending the group discussions organized by various estate planning professionals. Often, the "war stories" generated at these meetings can provide some real practical guidance.

Conclusion

CPAs are uniquely suited to participate in clients' estate planning and administration, and can be extremely valuable in minimizing the wealth-transfer tax burden of future generations. Further, you will find your practice can be greatly enhanced by the added services which such participation entails. ☑

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